

Effective from 1 January 2014

These changes explain the operation of paragraph 13.1d) of the Terms of Reference, which was inserted with effect from 1 January 2014.

New text is highlighted in yellow. Text which has been deleted is crossed out and highlighted in yellow.

Paragraph 13.1: Debt recovery or other proceedings

13.1 Debt recovery or other proceedings

- a) Subject to paragraph b), where an Applicant lodges a Dispute with FOS, the Financial Services Provider:
 - (i) must not instigate legal proceedings against the Applicant relating to any aspect of the subject matter of the Dispute;
 - (ii) must not pursue legal proceedings relating to debt recovery instituted prior to the lodging of the Dispute with FOS save to the minimum extent necessary to preserve the Financial Services Provider's legal rights and, in particular, must not seek judgment in the proceedings provided the Dispute is lodged before the Applicant takes a step in those legal proceedings beyond lodging a defence or a defence and counterclaim (however described); or
 - (iii) must not take any action to recover a debt the subject of the Dispute, to protect any assets securing that debt or to assign any right to recover that debt,while FOS is dealing with the Dispute.
- b) Notwithstanding paragraph a), with FOS's agreement and on such terms as FOS may require, the Financial Services Provider may:
 - (i) issue proceedings where the relevant limitation period for such proceedings will shortly expire – but those proceedings may not be pursued beyond the minimum necessary to preserve the Financial Services Provider's legal rights; or
 - (ii) exercise any rights it might have to freeze or otherwise preserve assets the subject of the Dispute.
- c) If the Dispute is subsequently decided by FOS and becomes binding upon the Financial Services Provider, the Financial Services Provider will abandon any aspect of proceedings against the Applicant that are inconsistent with that decision.

- d) Paragraph 13.1(a)(ii) does not apply to legal proceedings relating to debt recovery against a small business where the contract provides for a credit facility of more than \$2,000,000.

The guideline to paragraph 13.1 addresses the following issues:

- *When must an FSP (financial services provider) stop pursuing legal proceedings relating to debt recovery?*
- *How does paragraph 13.1a)(ii) operate?*
- *How does FOS identify Disputes where legal proceedings relating to debt recovery have been commenced?*
- *How does FOS handle these Disputes?*
- *What steps must an FSP take when notified of such a Dispute?*
- *When must an FSP set aside a judgment?*
- *How can an FSP raise questions about FOS's jurisdiction to consider a Dispute?*
- *What actions must an FSP take to stay or discontinue any proceedings?*
- *What is the expedited dispute resolution process for Disputes within FOS's jurisdiction?*
- *What happens if an FSP fails to comply with the time frames under the expedited process?*
- *What happens if an FSP fails to comply with FOS's requirements for stays, discontinuance or setting aside of court proceedings?*
- *What happens if an Applicant fails to comply with FOS's requests?*
- *When may an FSP reinstate proceedings?*
- *Can FOS consider Disputes about legal costs associated with legal proceedings relating to debt recovery?*
- *To what type of debt recovery action does paragraph 13.1a) apply?*
- *What is the exception to paragraph 13.1a)?*
- *What limits might FOS impose on debt recovery action?*
- *How are the ACCC and ASIC debt collection guidelines taken into account?*

General guidance on legal proceedings and other action by FSPs

The TOR stop FSPs from taking certain legal proceedings and other action against Applicants.

In disputes about Traditional Trustee Company Services, the TOR also stop FSPs from taking certain legal proceedings and other action against Other Affected Parties. The meanings of "Traditional Trustee Company Service", and "Other Affected Party" are explained in the guidelines to paragraphs [4.2b\)\(ix\)](#) and [14.1](#).

While FOS is dealing with a Dispute lodged with it, the FSP must not:

- instigate proceedings against the Applicant relating to the subject of the Dispute;

- pursue legal proceedings relating to debt recovery instituted before lodgement (unless the Applicant has taken a step in those proceedings beyond lodging a defence or a defence and counterclaim); or
- take action to recover a debt that is the subject of the Dispute, to protect assets securing that debt or to assign any right to recover that debt.

There is an exception to the stop outlined above. With our agreement, and on such terms as we may require, the FSP may:

- issue proceedings for which the limitation period will expire shortly; or
- exercise rights to preserve the assets the subject of the Dispute.

Most of the guidance provided in this section relates to paragraph 13.1a)(ii), which stops FSPs from pursuing debt recovery proceedings instituted before lodgement. Other matters covered in this section are:

- what amounts to “debt recovery” action for the purposes of paragraph 13.1;
- the process followed where an FSP seeks to rely on the exception to the stop; and
- the ACCC and ASIC debt collection guidelines.

Guidance on paragraph 13.1a)(ii)

When an FSP must stop pursuing legal proceedings relating to debt recovery

When a Dispute is lodged, paragraph 13.1a)(ii) prevents the FSP from pursuing legal proceedings relating to debt recovery that were instituted before the Dispute was lodged. The limitation applies from the time of lodgement – not from the time when FOS notifies the FSP of the Dispute.

Paragraph 13.1a)(ii) states that, in particular, FSPs must not seek judgment in the legal proceedings. As explained below, if an FSP contravenes this provision by obtaining judgment after a Dispute is lodged, the FSP must apply to set aside the judgment at no cost to the Applicant.

While paragraph 13.1a)(ii) requires that an FSP must stop the legal proceedings from the time the dispute is lodged, from a practical viewpoint, we regard the obligation on an FSP to refrain from taking any further steps in the legal proceedings commences from when an FSP is notified by FOS that a dispute has been lodged.

Therefore, if an FSP contravenes this provision innocently, because it is unaware that a dispute has been lodged with FOS, this will not of itself constitute “serious misconduct” under paragraph 11.3 of the Terms of Reference. Paragraph 11.3 requires that FOS report all serious misconduct to ASIC.

Exception to the ban on legal proceedings relating to debt recovery – small business loans exceeding \$2 million

Paragraph 13.1d) provides an exception to the ban on continuing legal proceedings under paragraph 13.1a)(ii). The exception applies when the proceedings relate to debt recovery, the Applicant is a Small Business, and contract (not including linked credit contracts) provides for a credit facility of more than \$2 million. A credit facility may include a loan, lease, related guarantee or other debt instrument which may give rise to a repayment obligation.

This means that FOS will not consider the dispute of a Small Business Applicant involved in legal proceedings with the FSP where the documented amount of the credit facility (based on the contract or other variation documentation) exceeds \$2 million and it will therefore be excluded under paragraph 5.2 a) of our Terms of Reference. The Small Business Applicant will need to defend the legal proceedings and bring a counterclaim if it wishes to pursue its claim against the FSP. Lodging a dispute with FOS will not prevent the FSP from entering judgment if the Small Business Applicant has not taken steps to protect their position in the court proceedings.

Scenarios for the application of 13.1(d):

Where the Applicant is a Small Business and the FSP had issued debt recovery legal proceedings against the Small Business prior to the Dispute being lodged with FOS, excluding the Dispute under 13.1(d) will not apply in the following situations:

- Documented credit facility of less than or equal to \$2 million (even if the balance owing is currently greater than \$2 million);
- Original credit facility was greater than \$2 million, but a more recent variation contract has reduced the facility to less than or equal to \$2 million;
- Where there are 2 documented credit contracts less than or equal to \$2 million even if the combined balance owing to the facilities is greater than \$2 million

If the dispute falls within jurisdiction FOS will require the FSP to refrain from pursuing the legal proceedings.

FOS will not require the FSP to halt legal proceedings, and the Dispute will instead fall *outside* jurisdiction, in the following situations:

- Documented credit facility is greater than \$2 million (even if the balance owing is currently less than or equal to \$2 million or the credit limit has since been cancelled)

Where the Applicant is a guarantor of a small business facility and the FSP had instigated debt recovery legal proceedings prior to the dispute being lodged with FOS against the Small Business and the guarantor, excluding the dispute under paragraph 13.1(d) will not apply where the credit facility is less than or equal to \$2 million.

Where the dispute is lodged by a guarantor of a small business facility and the FSP has issued proceedings against the guarantor but not the business because the business is

under external administration, excluding the Dispute under 13.1(d) will not apply in the following situations:

- Documented credit facility of less than or equal to \$2 million;
- The guarantor wishes to reduce their liability under the guarantee by the amount of a claim the small business may have against the FSP, and the documented credit facility is less than or equal to \$2 million;
- The documented credit facility is greater than \$2 million, but the remaining debt is under \$280,000 and the guarantor says they are not liable because the guarantee is for some reason unenforceable.

How paragraph 13.1a)(ii) operates

The phrase “legal proceedings relating to debt recovery” means a proceeding commenced in a court by an FSP to obtain judgment for a debt, or for recovery of possession of an asset provided by a debtor or guarantor as security for a credit facility.

An Applicant who lodges a defence or a defence and counterclaim and subsequently lodges a Dispute with FOS, will not be excluded from FOS’s jurisdiction unless the Applicant takes a further step in the proceeding. However, FOS will require the Applicant to provide an undertaking to stay any counterclaim they have filed. If this is not possible, then the Applicant will need to discontinue the counterclaim at their own cost.

If an Applicant does take a further step in the proceedings beyond lodging a defence or a defence and counterclaim, then FOS will consider that the court is a more appropriate place to deal with the dispute under paragraph 5.2a) of the Terms of Reference and the dispute will be outside of FOS’s jurisdiction.

An Applicant will not be regarded as having taken a “step” in the legal proceedings relating to debt recovery if they attend a directions hearing or agree to consent orders of a procedural nature only being filed in those proceedings.

Identifying Disputes where legal proceedings relating to debt recovery have been commenced

FOS seeks to identify Disputes where legal proceedings relating to debt recovery have been commenced prior to the Dispute being lodged by:

- asking the Applicant in the online Dispute Form whether (to their knowledge) the FSP has issued legal proceedings against them in a court; and
- where a Dispute Form is not completed at the time a Dispute is lodged, reviewing the information and documentation provided to identify whether legal proceedings appear to have been issued.

In the usual course, FSPs should receive notification that a dispute has been lodged with FOS by an Applicant within several hours of lodgement if the dispute is lodged

online or telephone and, generally, within two to three business days if it is lodged in writing.

If an Applicant or FOS identifies that legal proceedings appear to have been commenced by an FSP, FOS treats the Dispute as urgent and an expedited process applies.

If it is not apparent from the information and/ or documentation provided to FOS at the time of lodging the Dispute that legal proceedings have been commenced, the Dispute will be handled in accordance with our standard dispute resolution process. In these circumstances, the FSP must inform FOS as soon as possible after being notified by FOS that a Dispute has been lodged that legal proceedings relating to debt recovery have been commenced. This action is required to ensure that the expedited process applies.

FOS approach to handling Disputes where it appears legal proceedings relating to debt recovery have been commenced

When FOS becomes aware that legal proceedings relating to debt recovery have been commenced, it will expedite the dispute resolution process. The steps of the expedited process include:

- FOS will provide email notification to the FSP that the Dispute has been lodged ('notification of the Dispute');
- where appropriate, a senior FOS staff member will consider whether the Dispute is within FOS's jurisdiction; and
- unless the matter is clearly outside FOS's jurisdiction, FOS will refer the Dispute to the FSP for a response ('referral of the Dispute'). Details of the Dispute will be provided at that time.

Steps to be taken by the FSP as soon as possible upon receiving notification of the Dispute

Upon receiving notification of the Dispute, the FSP should have a process in place which ensures that no further steps are taken as soon as possible (with time being of the essence).

Setting aside a judgment

As the critical date is the date of lodgement of the Dispute with FOS, any judgment obtained after that date must be set aside by the FSP at no cost to the Applicant. Within 14 days of the referral of the Dispute, the FSP must apply to set aside the judgment.

The requirement to set aside the judgment applies even if the Dispute is subsequently considered to be outside of FOS's jurisdiction. This is because an Applicant may not have entered an Appearance or Defence because they had lodged a dispute with FOS. The Applicant should therefore be provided with an opportunity to do so once our file is closed.

Where the FSP must apply to set aside any default judgment, the FSP must confirm with FOS that it has made such an application. In appropriate cases, FOS may require the FSP to provide:

- a copy of the application within 14 days of the referral of the Dispute; and
- a copy of any subsequent order setting aside the judgment within 14 days of receiving the order from the court.

Raising questions about jurisdiction

If the FSP considers the Dispute to be outside FOS's jurisdiction, it should make a written submission to FOS within 14 days of the referral of the Dispute. FOS will consider this submission promptly and if a decision is made to exclude a Dispute, then the process for excluding Disputes contained in paragraph 5.3 of the TOR will apply. This includes providing an Applicant with 30 days to object to an assessment about our jurisdiction to consider the Dispute during which time our file will remain open.

Where an FSP has obtained judgment against an Applicant for repayment of a debt or possession of a security property prior to the date the Dispute is lodged, FOS is unable to consider a dispute about the FSP's entitlement to recover the debt or the security under paragraph 5.1(l) of the Terms of Reference.

FOS will require FSPs to provide copies of legal documents to establish that the FSP has obtained judgment against the Applicant in relation to the debt(s) or property(ies) in dispute. This would include a copy of the Statement of Claim and judgment.

Further, if the court documents are not clear about the accounts the legal proceedings related to, we may require an FSP to provide information to show that the legal proceedings actually related to the debt in dispute.

Importantly, FOS expects that an FSP will not take any steps to enforce a judgment until after our file is closed. If an FSP takes a step to enforce a judgment while our file is open, we may report this to ASIC as "serious misconduct".

However, parties should be aware that FOS has no power to stop a sheriff from executing an order or judgment. Therefore, lodgement of a dispute will not result in a sheriff being prevented from taking enforcement action. Nor will FOS require an FSP to withdraw an instruction already communicated to a sheriff to enforce a judgment or court order. In these circumstances, the applicant should seek urgent legal advice about any options which may be available to them.

Staying or discontinuing proceedings

If the Dispute is within FOS's jurisdiction, the FSP must stay the proceedings, at no cost to the Applicant. The stay must apply until our file is closed. If a hearing date has been set down, the FSP must adjourn the hearing date from time to time until our file is closed.

A formal order staying the proceedings, where this is not required by the relevant court rules, is not necessary if the FSP provides an undertaking to FOS to take no further steps in the proceedings. Within 14 days of the referral of the Dispute, the FSP must provide to FOS an undertaking in writing not to take a further step in the proceedings until our file is closed.

If a stay, adjournment or undertaking is not possible due to relevant court rules, the proceedings must be discontinued at no cost to the Applicant.

The Applicant must consent to a stay, adjournment or discontinuance of legal proceedings. If the Applicant does not consent, then our file will be closed.

Some court rules provide that when a Notice of Discontinuance is filed, the defendant can apply for costs. Where FOS requires the FSP to discontinue the proceedings and the FSP must file a Notice of Discontinuance, the Applicant must first agree that they will not seek costs from the court. This does not prevent the Applicant from claiming costs incurred in the legal proceedings as part of the Dispute lodged with FOS. If the Applicant does not agree to this requirement, then we will close our file.

In addition, paragraph 13.1a) (ii) does not prevent an FSP from complying with a court order requiring an interlocutory step to be taken by the FSP (for example, filing an affidavit of documents) as long as that step does not require the Applicant to take another step in the proceedings. See also the section below under the heading 'Exceptions to stop on debt recovery action' which outlines actions that may be allowed by FOS in exceptional cases.

Serving proceedings

An FSP must not serve proceedings unless an FSP considers it is necessary to preserve its legal rights. In these circumstances, we would require the FSP to request FOS's consent to serve the proceedings and to provide reasons to support its submission that it is necessary to serve the proceedings in order to preserve the FSP's legal rights. If FOS agrees for the proceedings to be served, the FSP will need to communicate to the Applicant that:

1. The dispute will continue to be considered by FOS but the FSP considers that service of the proceedings is a necessary step to preserve the FSP's legal position;
2. The FSP will not enter default judgment while FOS's file is open and the Applicant will not be required to take any steps in response to the proceedings; and
3. After FOS's file is closed, the FSP will provide the Applicant with the same amount of time that is provided under the relevant court rules to lodge a

defence after FOS closes its file. The FSP will consent to any application to the court required to give effect to this requirement

This information will avoid confusion for Applicants about whether they need to take any action in response to the proceedings or seek legal advice.

Dealing with Disputes within jurisdiction

The FSP must provide a written response addressing the issues in dispute within 14 days of either:

- the referral of the Dispute, where no submissions have been made about jurisdiction; or
- FOS's decision that the Dispute is within jurisdiction where submissions have been made about jurisdiction.

The Dispute will be reviewed and a conciliation conference by telephone will be set down as a matter of priority in an attempt to facilitate a timely and efficient resolution of the Dispute. Participation in the telephone conciliation will be compulsory for all parties to the Dispute. Where the Applicant has appointed an agent, both the Applicant and agent must attend. Where the Applicant will not participate in the telephone conciliation, our file will be closed. Where the FSP will not participate in the telephone conciliation, the Dispute will no longer be expedited.

If the Dispute is not resolved within seven days of the date of the conciliation conference, the Dispute will be investigated by a FOS caseworker as a matter of priority and a decision on the merits will be reached. The response timeframes for both the FSP and the Applicant during the investigation will be shorter than the timeframes which apply to a Dispute that is not expedited.

FSP's failure to comply with the time frames under the expedited process

If the FSP:

- fails to comply with the timeframes for the provision of a response; or
 - requests an extension of time to respond to FOS,
- the Dispute will no longer be dealt with using the expedited process. In such cases, the Dispute will be dealt with in accordance with the usual dispute resolution process and standard timeframes will apply.

FSP's failure to comply with FOS requirements for stays, discontinuance or setting aside of court proceedings

If the FSP:

- fails or refuses to stay, adjourn or discontinue the proceedings when FOS notifies the FSP that a dispute has been lodged by the applicant;
- breaches an undertaking to FOS to stay, adjourn or discontinue the proceedings;

- fails or refuses to set aside a judgment obtained after lodgment but before notification of the Dispute;
- proceeds to enter judgment even though it has received notification of the Dispute; or
- seeks to reinstate the proceedings while our file is still open; or
- seeks to serve proceedings without FOS's consent;
- seeks to enforce judgment after FOS notifies the FSP that a dispute has been lodged by the Applicant;

then FOS may:

- report the FSP to ASIC for serious misconduct under paragraph 11.3 of the TOR; and/or
- cancel the FSP's membership of FOS; and/or
- require the FSP to discontinue the legal proceedings.

Applicant's failure to comply with FOS requests

Where an Applicant fails to comply with FOS timeframes for the provision of information or a response, FOS will notify the Applicant that:

- they have a final opportunity to provide the information requested;
- if the information is not provided, we will close the file;
- we will only re-open the file if there are exceptional circumstances and
- FOS will also close the file if, in the opinion of the Ombudsman, the Applicant is not acting in good faith by seeking to delay the consideration of the dispute by FOS or not complying with FOS's dispute resolution process.

Reinstatement of proceedings when our file is closed

When we close our file because the Dispute is not within our jurisdiction or because the Applicant does not:

- attend the compulsory conciliation conference;
- provide requested information after receiving a final warning; or
- respond to a Recommendation or accept a Determination pursuant to section 8 of the TOR;

the FSP can continue with the legal proceedings which were commenced prior to lodgement of the dispute. If the Applicant intends to defend the proceedings, they should obtain legal advice as soon as possible about what options are available to them to protect their interests in the legal proceedings.

We will incorporate a warning to Applicants about an FSP's entitlement to continue with legal proceedings in our letters to Applicants advising them that we will be closing the file on a certain date. We will also encourage them to seek legal advice.

Where our file has been closed because an Applicant has not complied with our dispute resolution process or because the Ombudsman has formed the opinion that the Applicant is not acting in good faith, our file will not be re-opened, unless there are exceptional circumstances.

Legal costs

Where an issue in dispute is:

- the FSP's contractual right to recover the cost of legal proceedings from the Applicant (for example, whether the FSP's legal costs were reasonably and properly incurred); or
- whether the Applicant should not have had to incur legal costs as a result of legal proceedings being issued,

FOS may deal with these issues as part of its investigation of a Dispute.

FOS is unable to consider a dispute about legal costs which have already been awarded by a court. This is because FOS does not have the power to overturn a court judgment. However, we may consider a dispute that the costs charged to an Applicant's account exceeded the costs awarded by the court and were not reasonably and properly incurred. This is because, to the extent that the FSP is seeking more for costs than the amount awarded by the court, it does so pursuant to a contractual provision which is subject to an implied limitation that such costs are reasonably and properly incurred.

However, the FSP will not be entitled to recover legal costs at any time (whether pursuant to the contractual right, court order or otherwise) for:

- staying, adjourning or discontinuing the proceedings;
- setting aside any default judgment;
- making submissions about FOS's jurisdiction to consider the Dispute; or
- dealing with the Dispute; or
- an application for leave by the Applicant to file a defence or defence and counterclaim where the time limit for filing of these court documents was after the date that on which the Applicant lodged the Dispute.

This is because these costs were incurred by the FSP in dealing with a dispute lodged with FOS and, as a service which is free to consumers, should not be passed on to consumers.

Debt recovery action to which paragraph 13.1a) applies

Paragraph 13.1a) applies to action to recover a debt including:

- debt recovery through the court system;
- non court debt recovery processes;
- informal collection activities such as telephone calls;
- threatening to take legal proceedings to recover a debt;
- conducting repossession activities;
- seeking judgment for a debt or pre-judgment remedies such as orders to prevent the removal of property from the jurisdiction;
- issuing a letter of demand;
- assigning a debt; and

- making a credit listing with a credit reporting agency.

The stop on debt recovery action extends to action by an agent, employee or other person on behalf of an FSP. FOS treats debt recovery action taken on behalf of an FSP as action taken by the FSP.

The exception to paragraph 13.1a) – action that FOS may allow

There is an exception to the stop discussed above. We will allow an FSP to take two forms of action if FOS agrees and in accordance with any requirements imposed by FOS.

The two forms of action allowed under the exception are:

- issuing proceedings where the relevant limitation period will shortly expire (which may only be pursued as far as necessary to preserve the FSP's legal rights); and
- preserving assets that are the subject of the Dispute.

In addition, where the proceedings relate to debt recovery and have been issued before the Dispute was lodged, and the Applicant has taken steps in those proceedings (beyond lodging a defence, or a defence and counterclaim) before the Dispute was lodged, the FSP will be allowed to continue those legal proceedings.

If an FSP wants to take action to preserve its legal rights or assets relying on the exception to the debt recovery stop, it should write to FOS:

- requesting FOS to agree to the action;
- explaining why the FSP considers the exception applies; and
- providing any information that might assist FOS to consider the request.

Before deciding whether to agree, FOS considers whether any other material might assist it to make the decision. If so, FOS seeks the material and, if it is obtained, takes it into account.

If FOS agrees to the FSP taking action, FOS will inform the FSP and the Applicant in writing that it agrees and of any requirements that FOS imposes.

If an FSP issues proceedings and FOS ultimately makes a Determination that, for example, the Applicant is not liable for money sought by the FSP in the proceedings, then, when assessing the Applicant's loss and the remedies available, FOS can take into account the Applicant's costs of defending the proceedings.

Limits on debt recovery action

As FOS is only likely to agree to debt recovery action to maintain the status quo, FOS may require the FSP not to take any further steps in the legal proceedings while FOS deals with the Dispute. In particular, FOS will not approve an FSP taking any steps towards obtaining judgment in a debt recovery action.

Where FOS has allowed an FSP to commence a limited recovery action and FOS then makes a decision on the Dispute, the FSP must not proceed with any part of the issued proceedings if to do so would undermine the FOS decision. For example, if FOS considered whether the Applicant owed the FSP money as part of the Dispute and decided that they did not owe the money, the FSP would not be able to continue to try to recover that money.

ACCC and ASIC debt collection guidelines

In applying paragraph 13.1, FOS takes into account section 23 of the Debt Collection Guideline issued by ASIC and the ACCC (see ASIC Regulatory Guide 96). That guideline urges creditors and debt collectors to ensure their systems and practices allow external dispute resolution in regard to debt collection to operate effectively. The ACCC and ASIC guideline states:

- an FSP must suspend collection activity relating to a Dispute referred to an EDR scheme while the scheme considers the Dispute;
- an FSP should not sell or pass on a debt to an external agent for collection while a scheme is considering a Dispute involving the debt; and
- if an FSP assigns the debt, the FSP should seek to:
 - unwind the debt assignment; and
 - ensure the assignee does not undertake collection activity or start legal proceedings until the scheme has resolved the Dispute (and then only if the scheme confirms the liability).